

U. S. NATURAL RESOURCES, INC.

IBLA 73-1

Decided October 17, 1973

Appeal from a letter decision by the Acting Director, Geological Survey, determining an oil and gas lease is not entitled to a royalty limitation of 12 1/2 percent on production from part of the land it covers.

Affirmed.

Geological Survey! ! Oil and Gas Leases: Royalties

A determination of the Director of the Geological Survey that certain land in an oil and gas lease was within the productive limits of an oil and gas deposit as of August 8, 1946, so that it is not entitled to the royalty limitation of 12 1/2 percent pursuant to section 12 of the Act of August 8, 1946, will not be set aside where it is not arbitrary or capricious and is supported by competent evidence, and the lessee does not demonstrate by a clear and definite showing that it was in error.

APPEARANCES: R. J. Fernandes, Beverly Hills, California, for appellant; David C. Branand, Esq., Office of the Solicitor, Washington, D. C., for the United States Geological Survey.

OPINION BY MR. RITVO

U. S. Natural Resources, Inc., is the holder of oil and gas lease Sacramento 019275(b). The land is situated in that part of Kings County, California, covered by the so! called Middle Dome Agreement, signed on August 1, 1933, by, among others, Bolsa Chica Oil Corporation, the predecessor in interest to appellant. The lease as issued provided for a royalty rate on production varying from 12 1/2 to 33 1/3 percent. The Mineral Leasing Act, as amended by section 12

of the Act of August 8, 1946, 60 Stat. 957, 30 U.S.C. § 226c (1970), (hereinafter referred to as section 12) provides that the royalty under all leases requiring payment in excess of 12 1/2 percent is reduced to 12 1/2 percent:

"* * * as to such leases or such part of the land subject thereto, and the deposits underlying the same, as are not believed to be within the productive limits of any oil and gas deposit, as such productive limits are found by the Secretary to exist on August 8, 1946 * * *"

Appellant by letter dated January 17, 1972, to the Director of the Geological Survey requested a determination that royalty be limited to 12 1/2 percent under section 12 as to all the lands in the lease. The Acting Director by letter dated February 3, 1972, determined that about 1043.88 acres of the 1163.88 acres in the lease were entitled to the limitation, while the remaining 120 acres were not. Upon request of appellant, the Acting Director by letter of May 5, 1972, modified his earlier determination by adding 50 acres to the area that was permitted the 12 1/2 percent limitation leaving 70 acres subject to a possible higher royalty.

The sole issue is whether the 12 1/2 percent royalty limitation ought to be granted to these 70 acres.

From its effective date of October 1, 1933, lease Sacramento 019275(b) has been subject to the Kettleman Middle Dome Unit Agreement, approved September 30, 1933. The unit agreement was established following a discovery of oil in a Teriblör (Miocene) sand known as the "Burbank Sand" in wells drilled and completed in the SW 1/4 Sec. 29 and E 1/2 E 1/2 Sec. 30, T. 23 S., R 19 E., M.D.M. The unit agreement established a participation area of some 1170 acres, known as the "Red Line area." The 70 acres in question are situated near the southeast end of the participating area.

In 1939, the lessee was granted relief from drilling and producing operations 1/ at the same time as all leases of land committed to the

1/ Pursuant to section 39 of the Mineral Leasing Act, added by the Act of February 9, 1933, 30 U.S.C. § 209 (1970), the suspension of both drilling and producing requirements also suspended rental payments.

unit agreement agreed to suspend drilling and producing operations. In 1942, relief from the drilling requirements was terminated on this and other leases in the unit. Relief from production requirements was continued until terminated as of January 1, 1948.

In January 1948, well 73-30V, in NW 1/4 SE 1/4 NE 1/4 sec. 30, which had been completed in the Temblor sand in 1936, and on which production was suspended on October 1, 1939, again became productive from the McAdams (Eocene) sands as a result of deepening operations. The discovery was determined to be a new deposit entitled to a royalty limitation of 12 1/2 percent pursuant to section 12. Since well 73-30V is within the participating area of the Middle Dome Unit agreement, lease Sacramento 019275(b) is allocated its share of production.

In denying the royalty limitation to appellant, the Acting Director stated:

The following described lands were not within the productive limits of any oil or gas deposit on August 8, 1946, and are entitled to a royalty limitation of 12 1/2 percent:

Township 23 South, Range 19 East, M.D.M.

Sec. 32 N 1/2 NE 1/4 NE 1/4, SE 1/4 NE 1/4 NE 1/4,
E 1/2 SE 1/4 NE 1/4

The following described lands were within the productive limits of the Middle Dome Field on August 8, 1946, and are not entitled to a royalty limitation of 12 1/2 percent with regard to all formations:

Township 23 South, Range 19 East, M.D.M.

Sec. 32 SW 1/4 NE 1/4 NE 1/4, W 1/2 SE 1/4 NE 1/4,
SW 1/4 NE 1/4

The above described lands which are determined not to be entitled to a royalty limitation of 12 1/2 percent were included in the participating area for the Middle Dome Unit as approved September 30, 1933. At that time, the lands were presumed to be capable of producing oil and gas, and production was allocated to Sacramento 019275(b). Although no oil or gas had been produced for several years prior to August 8, 1946, production on August 8, 1946, from within this participating area would have been allocated to this lease.

By letter dated June 14, 1949 * * * the subject lease is entitled to a royalty limitation of 12 1/2 percent on oil or gas produced from the McAdams sand of Eocene Age. A royalty limitation of 12 1/2 percent could also be allowed for discovery of other new deposits of oil or gas [43 C.F.R. 3103.3-4 (iii)] on the described lands. Requests for such determinations should be submitted after a discovery is made.

In effect, the Director held that while he could not grant a royalty limitation for all formations in the latter 70 acres, he pointed out that any newly discovered deposits of oil and gas would be eligible for one.

Appellant disputes the Director's determination that any of the land in the lease was within the productive limits of an oil and gas deposit as of August 8, 1946. The Director's determination will not be set aside unless the appellant can demonstrate by a clear and definite showing that it was in error, Jack C. Bradley, 11 IBLA 294 (1973); William J. Colman, 9 IBLA 15 (1973). To put it more positively, the Director's determination will be accepted if it is not arbitrary or capricious and is supported by competent evidence. Atlas Corporation, 74 I.D. 76, 85 (1967).

Before considering appellant's contentions on appeal, three provisions of the regulations are pertinent. First, the regulation on royalty from production, 43 CFR 3103.3-4(a)(3), paraphrases the language of section 12. Next 43 CFR 3100.7-1 reads:

Determination by Geological Survey.

The Director of the Geological Survey will determine the boundaries of the known geologic structures of producing oil or gas fields, and, where necessary to effectuate the purposes of the act, the productive limits of producing oil or gas deposits as such limits existed on August 8, 1946.

Finally, 43 CFR 3100.7-4, reads:

Request for determination.

Any lessee or his operator may apply to the Director of the Geological Survey for a determination whether the land in his lease is inside or outside the productive limits of a producing oil or gas deposit as such limits existed on August 8, 1946.

Appellant begins by asserting that the Acting Director made a determination other than the one required by section 12. The Acting Director found that the 70 acres "were within the productive limits of the Middle Dome Field on August 8, 1946, and are not entitled to a royalty limitation of 12 1/2 percent as to all formations." Appellant says that the Director must make a finding that the lands are not within the productive limits of a producing oil and gas deposit, a determination, it contends, that is quite different from one that land is within the productive limits of an oil and gas field.

We agree that the Acting Director's finding is not couched in the words of the statute. However, by first making a determination in the statutory language that some lands are entitled to a royalty limitation of 12 1/2 percent and then stating that others, i.e., the lands here in question, are not "* * * with regard to all formations * * *" and setting out which deposits would not be entitled to the royalty limitation, the purport of the Acting Director's determination is clear.

In any event, a lease cannot have a royalty limitation until the Director finds it is eligible for one. Since he has not done so, the lease is bound by the royalty provisions it now contains.

Next appellant urges that even if the Acting Director considered the proper issue, he reached the wrong conclusion. That is, his finding that the disputed acreage was within the productive limits of an oil and gas deposit as of August 8, 1946, is wrong as a matter of fact.

It points out that no oil and gas has ever been produced from section 32, that there was no production from the participating area in 1946, and that there was no producing oil and gas deposit on the geologic structures of the Middle Dome Unit for some years until well 73-30V was completed as a producer on January 8, 1948.

In reply, the Geological Survey asserts that land can be within the productive limits of an oil and gas deposit even if there is no production, as for example, where there are wells shut in for lack of market, for reworking, or to conserve a deposit. It then points out that from 1939 to August 8, 1946, production on the lease was suspended at the request of appellant's predecessor. It is inconsistent, it says, to argue that land in a lease was not within the productive limits of an oil and gas deposit at the time the lease was enjoying a suspension of production. It also asserts that the lands in issue were within the participating area of the unit as it was originally

established. It refers to appellant's statement in its brief that, "The apparent basis for participating area so established was a geologic! engineering projection of structured contours of the Kettleman Hills Middle Dome Anticline,." It calls attention to the fact that despite a provision in the unit agreement providing for a method of reducing it, the participating area was never changed. In fact, it notes that the resolutions of the Middle Dome Corporation have consistently stated that the evidence failed to disclose that any of the participating areas were commercially unproductive.

The appellant does not dispute the factual basis of the Geological Survey position. Thus, it is accepted that the participating area was defined on the basis of geologic interpretation of the contours of Middle Dome anticline, that production was attained within it from the Burbank sand, and its boundaries have never been changed, despite several opportunities to do so. In addition, the lessee requested and obtained relief from the production requirements of the lease before and through the crucial date.

These facts, in our opinion, amply support the Director's refusal to find that all formations in the lands in the lease are entitled to the royalty limitation and his conclusion that he would examine each discovery on its own.

The evidence appellant offers in support of its position is first, that eight wells were drilled, seven were abandoned or were in the process of being abandoned on the crucial date, and one was under consideration for deepening to find whether oil or gas could be produced from deeper horizons than have heretofore been produced. However, the fact that there was no production from a deposit on August 8, 1946, does not establish that the deposit was not productive particularly where the lessee had obtained a suspension of production.

Appellant also contends the productive limits of the oil and gas deposits, if there were any, did not extend to the lease at issue. In support, appellant points out that no well was ever drilled within the pertinent portions of the lease. There is, however, no requirement that the productive limits be established by drilling. Geologic evidence is sufficient.

In summary, the appellant has not made a clear and definite showing of error in the Acting Director's determination.

Therefore, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decision appealed from is affirmed.

Martin Ritvo
Member

We concur:

Joan B. Thompson
Member

Douglas E. Henriques
Member

